

VIEWS OF CLASSICAL SCHOOL OF POLITICAL ECONOMY ON THE INTERCONNECTION BETWEEN THE PROCESSES OF ACCUMULATION AND CONSUMPTION

Anna Myza, Ekaterina Lesnevskaya*

1. Introduction

Nowadays the industrial structure has outdated in Ukraine, which causes the uncompetitiveness of our economy. According to the experts, the share of the third technological mode in the structure of Ukrainian economy is 58%, more than 90% of Ukrainian output hasn't got modern technological equipment, which affects the competitiveness of domestic products and reduces consumer demand [1]. The process of capital accumulation characterizes the proportion and development of expanded reproduction, promotes the renewal of capital goods, which improves the structure of domestic production and provides enhancement in product competitiveness. In the current circumstances it is necessary to reform Ukraine's economy by seeking the best forms of capital accumulation, which match the changes taking place in the modern economy. Studying and researching the formation and following evolution of the theory of capital accumulation will allow to understand the meaning of scientific problems and find its optimal solution which will end up with carrying out a deep economic analysis of economic reality.

2. Literature review

The theory of capital accumulation and the interconnection between the processes of accumulation and consumption were studied in the works of such representatives of classical economic direction as Adam Smith, David Ricardo, Karl Marx, John. Mill. Among Ukrainian scientists who study the questions of accumulation and consumption, we can notice V. Aleksandrovu, O. Bolhovitinovu, A. Halchynskoho, V. Heytsya, A. Hrytsenka, P. Eshchenka, B. Kvasnyuka, S. Kireyeva, I. Kryuchkovu, V. Mandeburu, M. Melamed, W. Muntiyana, I. Malogo, A. Revenka, L. Fedulovu, L. Shablystu.

3. The main aim of the submitted research

The purpose of this article is to examine the interaction between the processes of the capital accumulation and consumption in the works of economists who represent the classical school of political economy, and to define the role of their achievements in historical retrospect.

4. The main results of the study

Classical political economy made a significant contribution to the theory of accumulation, in contrast to their predecessors – mercantilists and physiocrats – moving the focus of their research from the sphere of circulation into the sphere of production. Adam Smith and David Ricardo were the distinguished representatives of the classical school.

Adam Smith believed that accumulation of annual share of the product (i.e. added value) causes the expanding production and further growth of wealth.

According to Adam Smith, the proportion between the quantity of the consumed products and the quantity of population in the country determines the level of material wealth, which becomes higher, if the proportion becomes bigger. This proportion depends primarily on labor productivity

* © Anna Myza; Post-graduate student; Department of the Economic Theory; Odessa National Economic University; E-mail: <Avita18@yandex.ru>;

© Ekaterina Lesnevskaya; Senior lecturer of Foreign Languages Department; Odessa National Economic University; E-mail <katlev@ukr.net>.

and proportional division of the society into productive and non-productive class. Labor productivity determines the division of labor and the rate of capital accumulation. As a result, the progress of the society, the growth of wealth depends ultimately on the rate of accumulation and the ways of possible using of the capital. The higher the level of division of labor and accumulation, the more products can be produced. Adam Smith pointed out that the “invisible hand” of the market regulates itself the accumulation of the capital in the right amounts and directions.

The accumulation of capital, in the opinion of Adam Smith, is positioned as the result of the capitalist thrift, due to which the owner of capital goods directs profits to the needs of expanding production, not to the “eating way”. Adam Smith concludes that “the direct cause of the increase in the capital is savings, not labor. It is true that labor supplies items for saving by thrift, but, however, without their saving as a result of trifling the capital would never have increased” [2].

In the frames of the theory of capital accumulation, Adam Smith thought that the price of goods normally is determined by income. The value of the social product consists only of $v + m$. The scientist recognized that every entrepreneur transforms the part of his capital into capital goods, but he believed that the price of each product embodies ultimately in wages, profit and rent. So that the transferred value shouldn't be included either in the value of particular good or in the cost of national product. This approach was called “Smith's dogma” and was wrongly used by a number of representatives of classical economics. Reducing the value of the social product to the sum of income – wages, profits and rents – Smith didn't considered the transferred value of capital goods. Therefore, according to this statement, the process of the accumulation is reduced entirely to the increase in variable capital, which leads to the fact that the growth in the labor consumption takes place only in the scale of the capital growth. The contradiction between consumption and production is absent. Consumption does not limit production; expanded accumulation can be done without any conflict.

Such approach of A. Smith's research is explained by the absence of time limits, which are normally used for the calculation of national product and national income per year. Transferred value of production appears as the past years labour product. Therefore, the sum of incomes that is equivalent to the cost of the re-established value of the current year is always less than the value of the annual social product, which also takes into account the cost of previous years, transferred from the capital goods.

A. Smith points out that “although the entire annual product of land and labour of every country undoubtedly is ultimately intended to satisfy the consumption of the population and to supply their income, however, after having been received from the ground or from the production workers, it is divided into two parts. One of these parts – and often the biggest one is directed primarily to the reimbursement of the capital or to restore consumption goods, materials and finished products, which were deduced from the capital, the other part is used for owner's income creation as profit from its capital or from capital of any other person, as his land rent” [2].

Thus, Smith acknowledges that annual product of society includes the part, which is used for recovering the used capital, namely consumed in the production, and does not act as income for personal consumption purposes. This scientific fact acknowledged the presence in the value of the product not only income but also the transferred value of capital goods. However, A. Smith touched this statement only in the indirect way.

Adam Smith did not consider the fixed capital formation, which was a significant disadvantage of his theory.

Ricardo continued the tradition of classical political economy. His work “On the Principles of Political Economy and Taxation”, published in 1817, was the top book of the progressive ideology of industrial bourgeoisie of the industrial revolution period.

A positive feature of Ricardo's research is his assertion that capital – is the part of the country's wealth which is used by production and is composed of food, clothes, tools, raw materials,

machinery, etc., necessary for labour's work movement. He believed that capital is represented by capital goods, and by capitalist's costs on employees' wages. In contrast to Adam Smith, Ricardo linked the concept of the "capital" not only with the stock of material wealth but also with the turnover of value, and divided the capital into fixed and working.

Ricardo, as well as Adam Smith made the same mistake reducing the accumulation of capital exclusively to the accumulation of variable capital. He insisted on that thesis according to which the accumulation is the result of savings or increasing growth of income with its unchangeable spending. He supported the idea of capital accumulation, by which he meant the joining of income to the capital and its consumption by production workers. Ricardo divided capital into fixed and working, and the degree of durability of these components was used as basis of such division.

In contrast to Adam Smith, Ricardo claimed that the rate of profit is continuously declining due to wages growth and growing population need for consumer goods supply. "Profit has a natural tendency to decrease, because with the progressive movement of wealth and the society the necessary increase of food is obtained by exploring the bigger quantity of labour. Overvaluation of essential items and wages has its borders, so that when the wage becomes equal to the total revenue, capital accumulation ceases, because in such circumstances capital cannot give any profit, the need in labour increase will be absent, and the population will reach its highest point. In fact, far long before this era the low level of profit stops every capital accumulation, and almost all the product of the country, except workers' wages becomes the property of the landowners and collectors of tax and acres" [3].

That is, due to the decline of the labour productivity in agriculture the growth in the food prices will lead to the increase of the minimum wage, which will absorb an increasing share of the value of production, and as a result will cause the reduce of the profit rate. D. Ricardo made an emphasis on increasing in wages as the only possible cause of low profits. He feared that lower profit rate in the end will reduce the accumulation of capital, and he pointed out that government policy must encourage the pursuit of accumulation. Ricardo concluded that economic growth will eventually stop because the progress of the society requires an extra amount of food produced at the expense of using more and more labour. Ricardo added that periodic gravitational tendency of profit to fall is slowing due to the improvement in machinery, discoveries in science and technology. It allows to keep that part of the labour which is required for their introduction, and to reduce the price of consumer goods. Such technical improvements only weaken this tendency, but don't entirely negate it.

Ricardo didn't share the Smith's view on value. He pondered that, based on Smith's view, wages and profits can grow simultaneously, and he opposed to the Adam Smith's idea with his own argument that the value splits into incomes, but doesn't consist of incomes, and this assumption affects the proportion in which the value is shared between classes. However, analysing the accumulation Ricardo did not take into account the fixed capital, which allowed to make a conclusion about the probability of full realization of the total product.

Ricardo believed that as the capitalist production meets people's needs and there are no limits for productivity and demand expansion besides profit rate reducing he denied the possibility of general overproduction. However, the first crisis of overproduction occurred in 1825.

James Mill, a follower of David Ricardo, as a source of value considered not only the workers' labour, but also the work enclosed in the capital goods. According to his theory, both workers and capitalists each receive their part of produced commodity as equal commodity owners. The two main targets of political economy by John Mill are the consumption by the society and the supply ensuring, which influences on this consumption. He pointed out that "what is annually produced is annually consumed; or, what is produced in one year is consumed in the next year". According to Mill, the quantity of goods produced by any definite nation is equal to the demand for these products at every moment of time. J. Mill also admits that despite this equality, some products can be produced in quantities much higher or lower relatively to demand for these products.

J. Mill distinguished the productive and unproductive consumption. The things that are made by someone, belong to someone, and are used by their owner with a defined purpose. The scientist highlighted two such defined purposes: to use things for immediate enjoyment and to use things for profit obtaining. Using things for profit obtaining refers to the productive consumption, and using for immediate satisfaction refers to the non-productive consumption. Those that are used to obtain the final profit are represented in wages, machinery and raw materials. According to Mill, it is the fact of paramount importance, and those who ignore this fact, make mistakes in the understanding political economy's basis. What remains from the annual product for being invested in capital, is necessarily consumed, because for the capital purposes it should be reflected in the wages payment, during the raw materials purchase, in the finished product, or finally, in making similarly produced machinery, through payroll, or raw materials using. Mill assumed that in the political economy a year acts as a period which includes the renewable cycle of production and consumption. Some things are produced and consumed in a period which is less than a year. The others have a turnover considerably more than a year. Anyway, a period of the year is convenient because it is associated with other class production, which leads back to the agriculture [4].

Marx, considering the peculiarities of capital accumulation in conditions of free competition, criticized all those who agreed with Adam Smith's view. He identified gross national product with the sum of income of the society classes. Marx believed that because of this reason their judgments concerned the analysis of simple, not of the extended reproduction. He created his own all reproduction types analysis scheme, according to which all the economy was divided into two divisions – one division produced capital goods, and the other – consumer goods [5, p.593]. Marx stressed that accumulation is impossible without any expanded reproduction, but not every expanded reproduction acts as capital accumulation, in such role it appears only during certain historical era.

Criticizing Adam Smith, and basing on the definition of the components of value, Marx emphasized that the expanded reproduction does not involve the possibility of unlimited growth of production regardless of consumption growth. Extended reproduction means reproduction of the contradiction between production and consumption in a growing scale.

He criticized the vulgar doctrine of economic crises caused by a reason of under-consumption which is the result of demand lack for purchasing the quantities of goods at such prices which would surpass the costs of their production. The content of one of the under-consumption economic crisis scenarios is that due to their low wages the workers cannot buy the product produced by themselves at its value. As a result, the crisis can be overcome by stimulating the non-productive demand of the third parties (by T. Malthus).

According to another scenario of under-consumption crisis, the growth rate of consumption lies far behind the growth of production capacity, resulting from using invested part of the income. The formed surplus of capacity surpasses the actually existing demand. This causes a drop in investment, income decline and inhibition in economic development. That is, the nascence of the crisis is linked with under-consumption because of savings surplus. Marx also criticized all economists who, like Ricardo, recognized only "intermittent" not "general" overproduction.

In his "Capital" Marx highlights the causes that lead to the nascence of the crises of general overproduction by evaluating the processes of capital accumulation and income distribution.

According to the concept of K. Marx, steady capital growth is the main purpose of capitalistic production, but the rising of value constantly conflicts with the methods which help achieve this goal [5, p.636]. To produce more surplus value it is necessary to constantly expand the production of consumption value, which faces a limited purchasing power of workers because the technological progress leads to the increase in organic structure of capital, which causes a decrease of variable capital in the proportion. Reduce of the part of variable capital causes a decrease in purchasing power. Even not examining the strict proportions of the process of expanded production we can see that the limit of variable capital creates a narrow scope for extended reproduction.

5. Conclusions

Thus, the theory of accumulation, created by the classical political economy, reflected essential features and characteristics of the phenomenon which took place in the appropriate era of development of productive forces and economic relations. Analyzing the experience of their predecessors, K. Marx demonstrated that capital accumulation had the historical and socio-economical nature, but he also stressed that the expanded reproduction entail the exacerbation of the contradiction between production and consumption. Fruitful achievements of the classical school of economists made the basis for further research of the interconnection processes between accumulation and consumption, and the results of interconnection impact on the economic development of the country.

Results of the study will allow to identify the achievements of classical political economy, which were confirmed by statistics data and promoted real economic growth. Prominent representatives of the classical school – Adam Smith and David Ricardo – distinguished savings (in Adam Smith's opinion – capitalist thrift) as an important factor of capital accumulation. Indeed, the savings are the one of the potential opportunities of capital accumulation and deserve the extra attention of the economists, because in some countries, including Ukraine, there was a problem of incomplete savings transformation into the capital accumulation for a long time, and, consequently, the actual capital increase was significantly below potential.

Analysis of the classical school achievements will provide an explanation of the current economic reality and solving the urgent practical problems through disclosure of the rate of the consumption and accumulation proportion and identifying the characteristics of gross national income distribution between consumption and accumulation.

References

1. Express Edition: Capital investment in Ukraine during January-September 2015, Official site of the State Statistics Service of Ukraine, available at: <http://www.ukrstat.gov.ua> (ukr)
2. Smith, A. (2007), Inquiry into the Nature and Causes of the Wealth of Nations, available at: http://royallib.com/read/smit_adam/issledovanie_o_prirode_i_prichinah_bogatstva_narodov.html#782916 (rus)
3. Ricardo, D. (1955), On the Principles of Political Economy and Taxation, Gospolitizdat, Moscow, available at: <http://ek-lit.narod.ru/ric021.htm> (rus)
4. Mill, J. (1844), Elements of Political Economy, 3rd Edition, available at: http://socserv2.socsci.mcmaster.ca/~econ/ugcm/3ll3/milljames/elements.html#_1_35.
5. Marx, K., Engels F. (1955), Capital, Vol. 1, V. 23, Publishing house of political literature, Moscow, 900 p. (rus)

Summary

The article analyzes the views on interconnection between the processes of the capital accumulation and consumption submitted in the works of the most famous classical school of political economy representatives. Capital accumulation historical retrospect studying is very important for the modern economic situation in Ukraine. It might helps to improve the structure of domestic production through the seeking of the best forms of capital accumulation. Researching the formation of capital accumulation theory in its connection with consumption processes will allow understanding the main cause of the scientific problem and finding its optimal solution.

Keywords: capital accumulation; consumption; transferred value; national income; expanded reproduction.

JEL classification: P00

UD classification: 330

Date of acceptance 20.09.2015.